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NOT TO BE PUBLISHED IN OFFICIAL REPORTS

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

DBN NORTH BEACH, LLC, Plaintiff and Appellant, v. JOHN F. DEBS et al., Defendants and Respondents.	G039834 (Super. Ct. No. 06CC13221) O P I N I O N

Appeal from a judgment of the Superior Court of Orange County, Daniel J. Didier, Judge. Affirmed.

Coontz & Matthews and M. Stephen Coontz for Plaintiff and Appellant.

Stuart W. Knight for Defendants and Respondents.

Okazaki Law Offices and Brian K. Okazaki for Defendants and Respondents John F. Debs, Anne R. Debs, Craig Strickland and Harriet Strickland.

* * *

Prospective buyers brought this action against the sellers of commercial property after the cancellation of escrow. The fundamental sticking point between the two parties was a previously existing leasehold on the property and how rent should be set on that property. We agree with the trial court that the sellers did not breach the sales agreement and that the buyers cannot recover.

I

FACTS

Defendants, a number of individuals and trusts (referred to collectively as Debs or defendants)[1] are the owners of a parcel of real property in San Clemente (the property). In April 2006, plaintiff DBN North Beach, LLC (DBN) entered into a written agreement with Debs to purchase the property for $2,250,000. The parties agree that was adequate consideration for the property. In accordance with the sales agreement, DBN paid an initial deposit of $50,000 into escrow, which was later released to Debs. Prior to the sales agreement, DBN had informed Debs that its intent was to develop the property as a mixed residential and commercial development.

At the time of the sale agreement, the property was subject to a lease between Debs, as lessors, and Kook Hyoung Choi and Hong Sook Choi (the Chois) as lessees. The lease documents consisted of a written commercial lease and two amendments. The lease provided that the premises would be used for operating "a gourmet coffee, juice, sandwich and dessert shop, for uses normally incident to that purpose, and no other purpose." The second amendment to the lease stated that on July 1, 2006 and on January 1, 2016, the fixed minimum rent would be calculated using an

[1] Stuart K. Knight, the attorney who initially represented all defendants in this matter, passed away shortly before oral argument was originally scheduled in this matter. New counsel advised the court that it had not been able to contact Lucrecia S. Vail, one of the defendants. Vail is the trustee of the Lucrecia S. O'Keefe Revocable Trust, and one of the property's co-owners. As her interests are identical to those of the remaining defendants, and with no way to notify her, we allow the appeal to proceed without Vail's appearance.

appraisal method set forth in the original lease. At the time, the monthly rent was $4,210.50.

The lease stated: "The Minimum Rent for the Second Extended Term shall be set at the then prevailing market rental rate for similar commercial property in the South Orange County Area. The parties shall endeavor to reach an agreement as to the then prevailing rental rate ninety (90) days prior to the expiration of the First Extended Term. Should the parties be unable to reach an agreement . . . the rate shall be set by appraisal, pursuant to the procedure outlined below. . . ." In sum, the appraisal method involved each party selecting an appraiser. (In the event one party did not select an appraiser, the other party's appraisal would be conclusive.) Should the appraisers fail to agree on a fair market value, provisions were made for the appointment of a third, neutral appraiser, whose appraisal would then be conclusive.

DBN contacted the Chois on June 23 by letter, advising them of the pending sale. DBN stated that the rent would be reset as of July 1, based on fair market value. The letter stated, "Assuming [DBN] acquires the property, we can either (i) proceed to the appraisal process, or (ii) if you prefer, meet with you and see if we can come to a mutual agreement regarding market rent. Of course, until the purchase is consummated, any agreement would be subject to [Debs's] approval."

On June 29, DBN and Debs entered into a written agreement to extend the closing date from June 30 to September 29, 2006, in consideration for DBN's deposit into escrow of an additional $50,000. This deposit was released to Debs.

The Chois and DBN did not reach an agreement on the adjusted rent for the property. In a June 30 letter, DBN informed the Chois that they were proceeding with an appraisal. The letter further stated: "Until escrow is closed, DBN and [Debs] are jointly responsible for decisions and actions of the Landlord under your lease."

DBN's appraisal concluded that the fair market value of the property was $2,250,000. This amount was multiplied by 8 percent, arriving at a rent for the property

of $180,000 per year, or $15,000 per month. In August, DBN informed the Chois of the results of the appraisal by letter, and "sensitive to the magnitude of the rental increase [they] will be facing," offered them an option to terminate the lease in January 2007, until which time the rent would be $6,000 per month.

On August 25, Debs and the Chois hired another appraiser to assess the fair rental value of the Chois's existing use of the property. That appraisal, completed on September 5, stated that the fair rental value of the property was $4,466 per month. **(¶ 11)**~ Debs and Choi then orally agreed that would be the new rent on the property, and the Chois promptly paid the difference in rent retroactive to July 1.

DBN refused to complete the purchase of the property on the September 29 closing date. DBN notified Debs on September 28 that Debs was in breach of the sales agreement, but that DBN was still willing to buy the property if the rent issue with the Chois could be resolved. On October 19, Debs informed DBN that it was in breach by failing to close escrow. DBN objected to Debs's attempt to cancel escrow and again stated it was willing to complete the purchase if DBN was not required to take the property subject to the adjusted rent agreed to by Debs and the Chois.

On December 21, 2006, DBN filed a complaint against Debs for specific performance, breach of contract, intentional interference with contract, and intentional and negligent interference with prospective economic advantage. Debs agrees that DBN's complaint encompasses its argument that by obtaining a second appraisal, Debs breached the implied covenant of good faith and fair dealing. DBN sought the amount it had spent attempting to buy the property, in excess of $200,000.

The case proceeded to a bench trial. The trial court found against DBN, concluding that DBN had assumed the risk of the encumbering leasehold, and that Debs had done nothing wrong. Rather, "this transaction, while likely well intended, was a business deal that became infeasible, went bad and soured, through no fault, legal or otherwise, of the seller/defendant parties." DBN now appeals.

II

DISCUSSION

Standard of Review

DBN, somewhat startlingly, refers to the lease, rather than the sales agreement, as the relevant contract for determining standard of review. We disagree. The Chois are not parties to this lawsuit, and their lease with Debs is not the relevant contract. The document at issue between the parties is the sales agreement. The terms of the contract, however, are not in dispute. "The interpretation of a written instrument, even though it involves what might properly be called questions of fact . . . is essentially a judicial function to be exercised according to the generally accepted canons of interpretation so that the purposes of the instrument may be given effect. . . . It is . . . solely a judicial function to interpret a written instrument unless the interpretation turns upon the credibility of extrinsic evidence." (*Parsons v. Bristol Development Co.* (1965) 62 Cal.2d 861, 865; see also *New Haven Unified School Dist. v. Taco Bell Corp*. (1994) 24 Cal.App.4th 1473, 1483.) "When no extrinsic evidence is introduced, or when the competent extrinsic evidence is not in conflict, the appellate court independently construes the contract. [Citations.]" (*Founding Members of the Newport Beach Country Club v. Newport Beach Country Club, Inc.* (2003) 109 Cal.App.4th 944, 955.)

Breach of the Implied Covenant of Good Faith and Fair Dealing

DBN argues that Debs breached the implied covenant of good faith and fair dealing by proceeding with a second appraisal and orally agreeing to a new rental amount for the Chois. They first suggest this was a breach of the sales agreement, quoting the following provision: "Seller agrees not to execute any new, or amend or terminate any existing, Leases without Buyer's approval." DBN argues that Debs "entered into an agreement that the tenant could pay less than fair rental value." Perhaps recognizing that this argument is subject to attack for confusing the reset of rent subject to the lease's

existing terms with a new or amended agreement, DBN then argues that it does not matter if Debs's actions actually breached the sales agreement. Instead, they claim that Debs's actions breached the implied covenant of good faith and fair dealing.

"Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement." (Rest.2d, Contracts § 205; see *Carma Developers (Cal.), Inc. v. Marathon Development California Inc.* (1992) 2 Cal.4th 342, 371 (*Carma*).) The scope of the covenant can be difficult to define, but "[i]t is universally recognized the scope of conduct prohibited by the covenant of good faith is circumscribed by the purposes and express terms of the contract." (*Carma*, *supra*, 2 Cal.4th at p. 373.) "[U]nder traditional contract principles, the implied covenant of good faith is read into contracts 'in order to protect the express covenants or promises of the contract, not to protect some general public policy interest not directly tied to the contract's purpose.'" (*Ibid.*)

DBN argues that Debs violated the covenant because Debs made an agreement to "allow less rent than the Lease provided . . . ." This, however, requires that we accept unquestioningly DBN's appraisal over the one obtained by Debs. We are not required to do so. As the trial court pointed out, "The terms of the lease and common sense indicate that a resetting of the lease amount[] is to be according to 'fair market rental value' of the property as a coffee shop, as contemplated by the lease, not as bare land, on a "highest and best use" basis, as a mixed-use residential and commercial project." We agree. In *Wu v. Interstate Consolidated Industries* (1991) 226 Cal.App.3d 1511 (*Wu*), a similar provision regarding appraisal for fair market value was in dispute between a lessor and lessee. The court concluded that "the only reasonable interpretation of the term 'fair market rental value' as used in the lease is that rent is to be established with reference to the nature of the premises and the purpose for which it has been leased, a motion picture theater. Reading the lease as a whole so that each clause aids in the interpretation of the others (Civ. Code, § 1641), the intent was clearly that the rent be

based upon the use of the premises. The premises is not a generic commercial building, or raw land, which could be put to any number of uses within the sound commercial judgment of the lessee. It is specifically defined as the theater and its appurtenances. The lessee is only allowed to use the premises as a theater unless the lessor consents to another use. An interpretation that the rent during the option terms is to be based upon the highest and best use of the property despite the purposes for which lessor and lessee agreed it could be used, would be economically and commercially unreasonable and violate the intent of the parties. (Civ. Code, § 1643.)" (*Id.* at p. 1515.)

Given that Debs's actions were in accordance with the law with respect to the Chois, we find no violation of the implied covenant of good faith and fair dealing. The lease required a reset of the Chois's rent on July 1, and Debs's method of calculating that reset was in accord with the relevant law. Further, it did not impede the "purposes and express terms of the contract." (*Carma, supra*, 2 Cal.4th at p. 373.) DBN was, as the trial court found, a sophisticated developer who purchased the property aware of the encumbering leasehold. If DBN made incorrect assumptions about the method by which the Chois's rent was to be reset, the blame does not fall on Debs. We therefore find no breach of the implied covenant.

Equitable Ownership

All of DBN's remaining arguments — which relate to the validity and finality of their own appraisal as opposed to Debs — are premised on the argument that as of the moment the sales agreement was signed, DBN became the equitable owner of the property, entitled to stand in Debs's shoes with respect to dealing with the tenant.

First, we find no evidence in the record that this issue was raised to the trial court. "At the risk of sounding like a broken record, we again cite the general rule: '[A] party is precluded from urging on appeal any point not raised in the trial court. [Citation.]'" *In re Aaron B.* (1996) 46 Cal.App.4th 843, 846.)

Assuming for whatever reason that the issue is not waived, we find DBN's argument unpersuasive. "The doctrine of equitable conversion 'is a mere fiction resting upon the principle that equity regards things which are directed to be done as having actually been performed where nothing has intervened which ought to prevent such a performance.'" (*Parr-Richmond Industrial Corp. v. Boyd* (1954) 43 Cal.2d 157, 165-166.) "But there is no equitable conversion where the contracting parties demonstrate an intention to the contrary." (*Ibid.*) Here, DBN points to no evidence demonstrating that either party intended it to act as the equitable owner. DBN did not, for example, collect rent from the Chois — indeed, evidence shows that the Chois were paying rent to Debs. Nor is there anything in the record to show that DBN acted as other than a prospective, future landlord. Its first letter to the Chois stated: "Assuming [DBN] acquires the property, we can either (i) proceed to the appraisal process, or (ii) if you prefer, meet with you and see if we can come to a mutual agreement regarding market rent. Of course, until the purchase is consummated, any agreement would be subject to [Debs's] approval." This does not demonstrate an equitable ownership, merely a prospective future legal ownership once escrow closed.

Because DBN was not the legal or equitable owner, its arguments about why its appraisal was superior to Debs for the purpose of setting rent are simply meritless. As a mere prospective owner, DBN had no right to enforce its appraisal. Therefore, DBN can show no breach of any requirement or condition placed on Debs by the sales contract, and it has no right to recover. We agree with the trial court that "this transaction, while likely well intended, was a business deal that became infeasible, went bad and soured, through no fault, legal or otherwise, of the seller/defendant parties."

III

DISPOSITION

The judgment is affirmed. The defendants are entitled to their costs on appeal.

MOORE, J.

WE CONCUR:

RYLAARSDAM, ACTING P. J.

BEDSWORTH, J.